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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 247

HENDERSON SUPPLEE, JR., MRS. MARIE SUPPLEE DICKSON AND MRS. ELIZABETH S. KIRK, EXECUTOR AND EXECUTRICES OF THE WILL OF C. HENDERSON SUPPLEE, DECEASED, AND MRS. C. HENDERSON SUPPLEE, SURVIVING WIFE, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 181–188)[1] is not reported. The *per*

[1] Pursuant to stipulation (R. 194), the printed record for purposes of this petition consists of the appendix to petitioners' brief in the court below plus the proceedings in the court below.

curiam opinion of the Circuit Court of Appeals (R. 191) is reported at 119 F. (2d) 423.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered April 8, 1941 (R. 192). The petition for a writ of certiorari was filed on July 8, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether there is substantial evidence to support the finding of the United States Board of Tax Appeals that taxpayer's stock in the Franklin Trust Company of Philadelphia became worthless in the year 1931, rather than in 1932.

STATUTES AND REGULATIONS INVOLVED

Revenue Act of 1928, 45 Stat. 791:

> SEC. 23. DEDUCTIONS FROM GROSS INCOME.
>
> In computing net income there shall be allowed as deductions:
>
> * * * * *
>
> (e) *Losses by individuals.*—In the case of an individual, losses sustained during the taxable year and not compensated for by insurance or otherwise—
>
> (1) if incurred in trade or business; or
>
> (2) if incurred in any transaction entered into for profit, though not connected with the trade or business; or

(3) of property not connected with the trade or business, if the loss arises from fires, storms, shipwreck, or other casualty, or from theft.

* * * * *

(j) *Bad debts.*—Debts ascertained to be worthless and charged off within the taxable year (or, in the discretion of the Commissioner, a reasonable addition to a reserve for bad debts); and when satisfied that a debt is recoverable only in part, the Commissioner may allow such debt to be charged off in part.[2]

Treasury Regulations 74, promulgated under the Revenue Act of 1928:

ART. 171. *Losses.*—Losses sustained by individuals during the taxable year and not compensated for by insurance or otherwise are fully deductible (except by nonresident aliens, see section 213 and article 1051) if—

(*a*) Incurred in a taxpayer's trade or business, or

(*b*) Incurred in any transaction entered into for profit, or

(*c*) Arising from fires, storms, shipwreck, or other casualty, or theft.

Losses sustained by corporations during the taxable year and not compensated for by insurance or otherwise are deductible.

Losses must usually be evidenced by closed

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[2] The corresponding provisions of the Revenue Act of 1932, 47 Stat. 169, are identical with the provisions set out in the text.

and completed transactions. The basis for determining the amount of the deduction for losses is the same as is provided in section 113 for determining the gain or loss from the sale or other disposition of property. * * *

* * * * *

ART. 174. *Shrinkage in value of stocks.*— A person possesssing stock of a corporation can not deduct from gross income any amount claimed as a loss merely on account of shrinkage in value of such stock through fluctuation of the market or otherwise. The loss allowable in such cases is that actually suffered when the stock is disposed of. If stock of a corporation becomes worthless, its cost or other basis determined under section 113 may be deducted by the owner in the taxable year in which the stock became worthless, provided a satisfactory showing of its worthlessness be made, as in the case of bad debts. * * *[3]

* * * * *

STATEMENT

This case involves the income tax liability of C. Henderson Supplee for the year 1932, who has since died and whose interests are represented in this case by the petitioners.

The issue is whether the taxpayer was entitled to a deduction for the year 1932 by reason of the

[3] Articles 171 and 174 of Treasury Regulations 77, promulgated under the Revenue Act of 1932, are for present purposes identical with those set out in the text.

worthlessness of his investment in the Franklin Trust Company of Philadelphia. The Board of Tax Appeals found that the worthlessness had occurred in 1931 rather than in 1932, and the facts supporting that finding may be summarized as follows:

The taxpayer was a stockholder of the Franklin Trust Company of Philadelphia, which had closed its doors on October 5, 1931 (R. 14, 33, 183), and has never since reopened. Under date of June 29, 1931, the Banking Department of the State of Pennsylvania had examined the records of the Franklin Trust Company and had reported (Pet. Ex. 1) that the 300,000 outstanding shares of stock of the Trust Company of par value $10 per share, had a book value of approximately $21.50 per share (R. 9, 182). By the time the Franklin Trust Company closed, its portfolio admittedly had been "skimmed of a lot of the cream,"[4] (R. 34; cf. R. 156), and the remaining assets, such as real estate mortgages (R. 34–35), were nonliquid (R. 15). The general business situation in and around Philadelphia between October 5, 1931, and the end

[4] The Trust Company's difficulties had been accentuated, if not precipitated, by the closing on December 22, 1930, (R. 23) of the Bankers Trust Company of Philadelphia. The closing of the Bankers Trust led to a run on the Franklin Trust Company; in the course of this run, the Franklin Trust Company's loss of deposits amounted to approximately $15,000,000 (R. 14–15, 23, 182). To meet this sudden demand, the Franklin Trust Company had disposed of most of its quick securities (R. 24).

of 1931 "wasn't good." Rather than improving at that time, "it stayed at a low level" (R. 28; cf. R. 182).

The Board of Tax Appeals found (R. 182–183) that at or about the end of September 1931—

> The position of the Franklin Trust Co. was precarious. It had borrowed substantial amounts of money from the Philadelphia Clearing House Association, and asked for a further loan about the first of October. A Committee of the Clearing House Association made an examination of the Trust Company's books and determined that the Trust Co. was insolvent. It did, however, advance to the Trust Co., upon the security of its choicest assets, $1,000,000 [on Monday, October 5, 1931, to enable the Trust Company to open and do business that day].

(See also R. 41–42, 128, 133–134, 156.)

On October 5, 1931, three of the largest depositors in the Trust Company presented their demands for more than the one million dollars which had been advanced that morning by other banks through the Clearing House Association (R. 42, 133–134, 183). These demands were not honored on the ground that to pay them would be unfair to other depositors. The other banks in Philadelphia would advance no more funds to the Franklin Trust Company. At 12:01 A. M., October 6, 1931, the Company was placed in the hands of the Banking

Department of the Commonwealth of Pennsylvania (R. 14, 33, 42, 55, 57–58, 183).[5] The Company thereafter refused to receive deposits and ceased to operate as a commercial bank (R. 183).

After taking possession on the morning of October 6, 1931, the employees of the Pennsylvania Banking Department, under the supervision of Dr. Gordon, the Department's Secretary, "endeavored to hastily prepare" an inventory of the assets and liabilities of the Trust Company (R. 55). This was "merely an assemblage of book values," a "presentation of book values of assets and liabilities" and did not represent an attempt to appraise the assets (R. 56). The State Banking Department found that the Trust Company at the time it closed its doors had assets of a book value of $37,828,-146.43 and liabilities of $27,149,637.71; $11,031-123.35 of the liabilities were secured or offset by amounts due the Trust Company (R. 183).[6]

For some time after the Franklin Trust Company closed, some of its officers and stockholders worked on reorganization plans. These efforts continued to June 1932 (R. 18, 20–21, 33, 36, 43–44,

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[5] The Franklin Trust Company was one of the forty-four banks taken over by the Banking Department of Pennsylvania in October 1931 (R. 55, 65, 182).

[6] Notwithstanding these book figures the subcommittee of the Clearing House Committee, which had appraised Franklin Trust's assets a few weeks before, reported the Trust Company as insolvent (R. 128).

183),[7] but they proved futile (R. 33). "Not a penny" was secured toward reorganization and not even expenses were paid for the attorney of the Franklin Trust Company, who worked on the reorganization plans (R. 37).

Meanwhile, on December 15, 1931, the Secretary of Banking ordered the liquidation of the Trust Company (R. 47, 57, 183) because, he testified, the bank was unable either to meet its obligations or to raise additional money (R. 58).[8] No appraisal of the assets had been made at that time. The book value of these assets far exceeded the total liabilities of the Trust Company but it was apparent to all concerned that many of the assets had suffered a great shrinkage in value and many of them were unsalable (R. 183). According to the special deputy whom the Secretary of Banking placed in charge of the affairs of the Franklin Trust Company "when Dr. Gordon gave his liquidating order, personally, I had no hope" (R. 47).

From the October 1931 inventory (at book values) which was at hand at the time the Secretary of Bank-

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[7] The schemes for reopening all depended upon (a) persuading the large depositors to make no demands for their deposits for five or ten years, so that the Trust Company could work out its slow assets, and (b) bringing some new money into the organization (R. 33-34).

[8] The Secretary of Banking testified that he decided to issue the liquidation order without first determining the question of solvency "based on a factual appraisement of the market value of the assets" (R. 59).

ing ordered liquidation, it would have been impossible, the Secretary testified, for "any one on earth" to have "predicted values" of assets (R. 57). An appraisal was necessary for the purpose, but two or three months were required to prepare it (R. 56). Thus " * * * the relation between * * * assets and * * * liabilities was not definitely settled until the inventory and appraisement were filed in 1932" (R. 47). The appraisers filed their report[9] with the Secretary of Banking in June 1932 (R. 46, 183). The appraisal showed that the book value of the Trust Company's assets at the time the state authorities took possession was $37,828,146.43, but that the actual value of the assets was only $19,236,439.74. The appraisal showed total liabilities of $27,149,637.71, including offsets and secured liabilities of $11,031,123.35, leaving total net liabilities unsecured of $16,118,514.36. The total net available assets to meet such unsecured liabilities was $8,205,316.39 (Ex. 2; R. 183–184).

The liquidation of the Franklin Trust Company was still in progress at the time of the first trial, November 22, 1938. Stockholders had received

[9] The appraisal was prepared by Mr. Norman Hayes, a vice president of the Philadelphia National Bank, and Mr. Frank Felton, of the J. C. Jackson Realty Company, whom the Secretary of Banking had appointed as appraisers on January 18, 1932, to appraise the company's assets at their actual market value as of the date when the Franklin Trust Company closed (R. 21, 22, 46, 57, 71, 122, 183).

nothing. Dividends of from 30 cents to 40 cents on the dollar had been paid to depositors (R. 184). Although small additional dividends may be paid to the depositors, the total amount will be small (R. 184).[10]

On the basis of this evidence the Board of Tax Appeals found that the shares of stock of the Franklin Trust Co. became unsalable and absolutely worthless in 1931.[11] The Circuit Court of Appeals affirmed (R. 191) the finding and decision of the Board.

ARGUMENT

The decision of the court below affirming the determination of the Board of Tax Appeals was correct and there is no conflict with the decisions cited by the petitioners.

1. It has been repeatedly and uniformly held that the time when stock becomes worthless is a question of fact to which the substantial evidence rule applies.[12] *Foster* v. *Commissioner*, 112 F. (2d) 109,

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[10] During Dr. Gordon's term as Secretary of Banking, the Department of Banking had ordered 157 banks liquidated (R. 58, 64). In the case of only one of these banks was any payment made to the stockholders (R. 65; cf. R. 59).

[11] See also the Board's opinion (R. 187).

[12] Petitioners cite no case to the contrary. ~~Taxpayer~~ does, however, contend (Pet. 5) that this case involves a mixed question of fact and law, citing *Helvering* v. *Rankin*, 295 U. S. 123, 131; and *Helvering* v. *Tex-Penn Co.*, 300 U. S. 481, 491. The short answer to this is that neither case was concerned with the issue of when stock becomes worthless; they hold only that other issues of taxation sometimes do

113 (C. C. A. 1st); *Thompson* v. *Commissioner,* 115 F. (2d) 661, 662 (C. C. A. 2d); *Bartlett* v. *Commissioner,* 114 F. (2d) 634, 641 (C. C. A. 4th); *Brown* v. *Commissioner,* 94 F. (2d) 101, 103 (C. C. A. 6th); *Industrial Rayon Corp.* v. *Commissioner,* 94 F. (2d) 383 (C. C. A. 6th); *Rand* v. *Helvering,* 116 F. (2d) 929, 933 (C. C. A. 8th); *Bancroft* v. *United States,* 33 F. Supp. 225, 233 (C. Cls.).

The facts set forth in the Statement, *supra,* pp. 4–10, amply indicate that there is substantial evidence to support the Board's finding that the stock in the Franklin Trust Company "became unsalable and absolutely worthless in 1931" (R. 184). By October 5, 1931, the Trust Company had virtually stripped itself of liquid assets (R. 34–35); it was unwilling to meet the demand of its depositors (R. 42, 133–134, 183); it was determined to be insolvent by a committee of the Clearing House Association (R. 128); it could obtain no more funds (R. 42). On October 6, 1931, it was taken over by the Banking Department (R. 14, 33, 55, 57–58, 183). At

present a mixed question of fact and law. This we do not dispute. Further in support of the contention that something more than a question of fact is here involved, petitioners cite a series of Pennsylvania decisions holding that a receiver may be appointed for a corporation even though it is solvent (Pet. 6). But these cases are irrelevant to the issue whether this is a mixed question of fact and law. The Board of Tax Appeals did not hold that mere receivership as a matter of law results in worthlessness of the stock of a corporation, but based its conclusion on many facts not limited to receivership.

that time, the Trust Company had assets of only $19,236,439.74 to meet liabilities of $27,149,637.71 (Pet. Ex. 2; R. 183–184). Throughout the remainder of the year 1931, it was unable to raise any funds whatsoever, and it could not even pay expenses to its attorney (R. 33, 37). On December 15, 1931, the Secretary of Banking ordered it liquidated (R. 47, 57, 183), and at that time, his deputy, who had been in charge of the company's affairs for over two months, "had no hope" (R. 47).

The Board's findings of fact, thus fully supported by substantial evidence, are conclusive on appeal. Cf. *Helvering* v. *Kehoe,* 309 U. S. 277, 279; *Helvering* v. *Nat. Grocery Co.,* 304 U. S. 282, 285, 294; *Elmhurst Cemetery Co.* v. *Commissioner,* 300 U. S. 37, 40; *Hulburd* v. *Commissioner,* 296 U. S. 300, 306.

2. Petitioners contend that five cases are in conflict with the decision of the court below (Pet. 3–4, 8–13). One of these allegedly conflicting cases was decided by a district court;[13] two by the Court of Claims;[14] and two by the Board of Tax Appeals.[15]

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[13] *Sherrill* v. *Adkins* (E. D. Ark.), decided December 2, 1939, not officially reported but found in 1940 C. C. H., Vol. 4, par. 9154.

[14] *Bancroft* v. *United States,* 33 F. Supp. 225; *Lyon* v. *United States,* 5 F. Supp. 138.

[15] *Terhune* v. *Commissioner,* 40 B. T. A. 750; *Watson* v. *Commissioner,* 38 B. T. A. 1026. In any event, even a squarely contrary decision of the Board does not constitute authority for reversing another decision of the Board. *Rogers* v. *Commissioner,* 103 F. (2d) 790, 793 (C. C. A. 9th).

But the issue of when stocks become worthless is entirely factual and must be resolved in each case by the facts disclosed by the particular record. The facts upon which each of these five cases turn differ substantially from the facts of the instant case. Moreover, each of these cases was decided by a tribunal of original jurisdiction, whereas the basic issue in the court below was simply whether the Board's findings were supported by substantial evidence.

CONCLUSION

The decision of the court below is correct, and there is no conflict of decisions. The case turns upon its own facts and presents no question of general application. The petition should be denied.

Respectfully submitted.

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